(3)

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1945.

No. 96.

LOUIS STOCKSTROM,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

PETITIONER'S REPLY BRIEF.

THOMAS R. REYBURN,
Attorney for Petitioner.

CHASE MORSEY,
RICHARD A. AUSTIN,
Of Counsel.

ST. LOUIS LAW PRINTING CO., 415 North Eighth Street. CEntral 4477.

INDEX.

Cases Cited.

Statute Cited.

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1945.

No. 96.

LOUIS STOCKSTROM,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Eighth Circuit.

PETITIONER'S REPLY BRIEF.

In the first sentence, under the heading "Argument", on page 11 of respondent's brief we find this statement:

> "The basic principles which govern the disposition of this case were settled by this Court in Helvering v. Clifford, 309 U. S. 331."

We believe that this statement is erroneous. We further believe that this fundamental error is the cause of

the conflict in many of the hundreds of cases which have been decided in the Tax Court and the various courts of appeal.

In the opinion in the Clifford case this Court said:

> "In absence of more precise standards or guides supplied by statute or appropriate regulations, the answer to that question must depend on an analysis of the terms of the trust and of the circumstances attendant on its creation and operation."

In footnote 1, which appears at the bottom of page 334 of the Clifford opinion, we find this statement:

> "We have not considered here Article 166-1 of Treasury Regulations 86 promulgated under Section 166 of the 1934 Act and in 1936 amended (T. D. 4629) so as to rest on Sec. 22 (a) also, since the tax in question arose prior to that amendment."

The principles which govern the disposition of this case were, therefore, not settled by this Court in the Clifford case, because the taxable years involved in this case are 1938, '39, '40 and '41.

In its opinion in the Clifford case this Court was careful to point out in the footnote that for taxable years beginning after 1936 the law would be found in Section 22 (a) and the Commissioner's Regulations promulgated thereunder.

In the Tax Court this point was passed by without notice.

The Circuit Court of Appeals refused to discuss it.

It is now ignored in respondent's brief.

We say that the law of this case is now governed by Sec. 22 (a) and the Commissioner's Regulations which were promulgated thereunder.

We further say that the principles announced in the Clifford case were limited by this Court to taxable years beginning prior to 1936.

The Regulations which were promulgated under Sec. 22 (a) are set forth in the appendix to the petition in this case, on pages 19-23. These Regulations, as pointed out by this Court, were not adopted until the year 1936 and hence had no application to the Clifford case, because the tax in that case was for the year 1934.

These Regulations clearly show that it was not the intention of the Commissioner that the petitioner in this case should be liable for a tax on the trust income, for the following reasons:

(a) The trusts are long-term trusts—the regulations cover only short-term trusts.

(b) Grantor stripped himself of the substantial incidents of ownership in the corpus.

(c) The grantor, incident to a definitive and permanent disposition of certain of his property, created the trusts in order to conserve the property, not for himself but for the donees.

The Commissioner's Regulations are rather lengthy but when read as a whole it is quite apparent that they do not cover long-term trusts. On page 22 of our petition there appears the following statement from the Commissioner's Regulations:

> "On the other hand, if the grantor, incident to a definitive and permanent disposition of certain of his property, creates the trust in order to conserve the property not for himself, but for the donees who will ultimately enjoy it, the provisions of Sections 161, 162 and 163 are applicable."

The Regulation then continues and cites examples (A), (B) and (C). These examples clearly show that it was the intent of the Commissioner, when writing these Regulations, that the income from trusts of the character now under consideration should not be taxed under Sec. 22 (a).

We have not been able to get the Tax Court or the Court of Appeals to give any consideration to these Regulations, and respondent's brief now before the Court utterly ignores the regulations.

In the last sentence on page 15 of respondent's brief there appears this statement:

> "The task of translating the Clifford doctrine into a specific criterion of tax liability in particular cases is primarily a matter for the Commissioner and the Tax Court."

In answer to this statement we say that the Clifford doctrine is applicable only to those cases wherein the tax liability arose prior to the date that the Commissioner adopted his Regulations under Sec. 22 (a). After these Regulations were adopted the law of the case is governed by Sec. 22 (a) and the Regulations promulgated thereunder.

It is the failure to recognize this important fact that has led the courts to announce so many conflicting decisions.

In the very case at bar it was Judge Johnson, the writer of the majority opinion, who said:

> "It is to be wished, of course, that the field opened up by the Clifford case may come to have some definite monuments."

This statement overlooks the fact that this Court established a monument and limited the Clifford doctrine to cases which arose prior to the adoption of the Commissioner's Regulations in 1936.

Judge Sanborn, who wrote the concurring opinion, said:

> "I think the Tax Court might well have decided this case in favor of the taxpayer, but the standard of determining to whom the income is taxable is presently so vague and indefinite that I have no conviction

> as to whether the decision of the Tax Court is, as a matter of law, right or wrong. I, therefore, concur. I think it is unfortunate that courts which are required to determine such controveries as this must express opinions which are obviously little more than guesses."

None of the opinions in any of the courts would be "guesses" if the courts followed the direction of this Court in the Clifford case, in footnote 1, page 334. In that footnote this Court said in substance that after the taxable year 1936 the law would be found in Sec. 22 (a) and the Regulations promulgated thereunder.

It ought to be an easy matter and not a "guess" to say whether or not the income from any trust is taxable to the grantor if the law were construed in accordance with the regulations. The difficulty in all of the cases is that the Commissioner, the Tax Court and the various courts of appeal have utterly ignored the Commissioner's Regulations.

On page 11 of respondent's brief we find this statement:

> "We do not share petitioner's views as to the existence of a conflict in the decisions of the Circuit Courts of Appeals upon this matter. Since Com. v. Katz, 139 Fed. (2d) 107, and Com. v. Armour, 125 Fed. (2d) 467, were affirmances of the Tax Court's decisions, they represent, at most, instances of differences in emphasis in the Tax Court's rulings in this field."

As we read this statement it amounts to an admission that there is a conflict in the decisions, but the conflict is due to "differences in emphasis in the Tax Court's decisions."

To illustrate, in the Armour case both the Tax Court and the Circuit Court of Appeals for the Seventh Circuit emphasized strongly the fact that the Clifford doctrine

did not apply to long-term trusts. In the case at bar the Tax Court and the Circuit Court of Appeals emphasized strongly the fact that the Clifford doctrine does apply to long-term trusts.

In the Armour case both the Tax Court and the Court of Appeals for the Seventh Circuit emphasized strongly the fact that adult children living separate and apart from the grantor were not members of his family group.

In the case at bar the Tax Court and the Circuit Court of Appeals emphasized strongly the fact that adult children living separate and apart from grantor are members of his family group.

These rulings, as pointed out by counsel for respondent, are not conflicting but are merely "differences in emphasis."

We belong to the old school and prefer to call them "head-on conflicts."

On page 14 of respondent's brief we find this statement:

> "Here, as in the Clifford case, the tax is levied upon income which in substance and reality is that of this taxpayer and not of another."

This statement overlooks two important facts:

1. In the Clifford case the property was to revert to the taxpayer in the short space of five years, while in the case at bar there is no reversion.

2. The income could not be that of this taxpayer in view of the specific finding of the Court of Appeals in this case that—

> "All ten of the trusts were irrevocable and petitioner was not to receive corpus or income from any of them. * * * The trusts were intended for petitioner's family and he was not to share in the income or get back any of the corpus."

As pointed out in our brief accompanying the petition, on page 13 thereof, the trust corpus and income were fully, finally and definitely disposed of. The money to pay the tax would have to come from petitioner's private property. This, in effect, would be the levying of a tax on capital and would have nothing whatever to do with income.

Under Point II, on page 10 of our brief accompanying the petition, we stated that the decision in this case is in conflict with the decision of this Court in the case of Helvering v. Stuart, 317 U. S. 154. Respondent in his brief does not deny this statement. It, therefore, stands admitted on this record that the decision of the Court of Appeals in this case is in conflict with the decision of this Court in the Stuart case.

In the Stuart case this Court said:

> "Economic gain realized or realizable by the taxpayer is necessary to produce a taxable income under our statutory scheme."

No one has ever been able to point out where or how, in this case, the petitioner could realize economic gain from the trust assets.

We desire to state that in the Tax Court we relied on the Stuart case but that court passed it by without comment.

When the case reached the Circuit Court of Appeals we called that court's attention to the Stuart case, but it, like the Tax Court, passed it by without comment.

There must be something in the Stuart case which the respondent, the Tax Court and the Court of Appeals for the Eighth Circuit cannot explain. All of them have adopted the easy way out and have refused to give any notice whatever to the Stuart case.

It is important to note that the Stuart case, like the Clifford case, involved taxable years prior to 1936 and

prior to the promulgation of the Commissioner's Regulations under Sec. 22 (a).

The major portion of the argument contained in respondent's brief is addressed to the proposition that the decision of the Tax Court in this case should be final and not subject to review by the appellate court. As an example, we quote from page 11 of the brief the following:

> "The process of applying the Clifford principle to specific factual situations is obviously within the special competence of the Tax Court."

This argument overlooks the fact that we are here attempting to construe a statute [Sec. 22 (a)] and the Regulations of the Commissioner promulgated thereunder. This is always a pure question of law and reviewable by the appellate courts.

In the late case of Trust u/w of Bingham v. Com., #932, last term, decided June 4, 1945, not yet reported, this Court said:

> "But whether the applicable statutes and regulations are such as to preclude the decision which the Tax Court has rendered, is, as was recognized in Dobson v. Com., a question of law reviewable on appeal."

It is the contention of petitioner that the applicable statute [Sec. 22 (a)] and the Commissioner's Regulations are such as to preclude the decision which the Tax Court has rendered.

This point was argued in the Circuit Court of Appeals but that Court based its decision squarely on the case of Dobson v. Com., 320 U. S. 489. It is, therefore, plain that petitioner has never had a hearing on the vital question of whether or not he is taxable on the income from the trusts under Sec. 22 (a) and the Commissioner's Regulations promulgated thereunder.

It is, therefore, of the utmost importance that the writ of certiorari be granted in this case in order that this Court may have an opportunity for the first time to review the many conflicting decisions on this troublesome question in the light of Sec. 22 (a) and the Regulations promulgated thereunder.

If this Court sees fit to grant the writ of certiorari it will afford the first opportunity to petitioner to have judicially determined the question of whether or not the

> "applicable statute and Regulations are such as to preclude the decision which the Tax Court has rendered."
>
> Trust u/w of Bingham v. Com., supra.

The decision in this case is out of line with the majority of the decisions on the taxation of trust income. In fact it is so far out of line that we are reliably informed the Commissioner is now engaged in rewriting his Regulations under Sec. 22 (a). In view of this fact it might not be inappropriate to request the Court to withhold any action on this application until the Commissioner has promulgated his new Regulations under Sec. 22 (a).

Respectfully submitted,

THOMAS R. REYBURN,
Attorney for Petitioner.

CHASE MORSEY,
RICHARD A. AUSTIN,
Of Counsel.